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SUBJECT: IRAN: EU EXPLAINS 1803 NEXT STEPS TO A/S O'BRIEN,
TREASURY

Classified By: USEU EconMinCouns Peter Chase for reasons 1.4 (b), (d),
(e).

[1](#). (S//NF) SUMMARY: U.S. Treasury Assistant Secretary for Terrorist Financing Patrick O'Brien met senior EU and Member State representatives on May 14 and 15 to stress the importance of EU action on sanctions against Iran. EU interlocutors explained the current EU implementation status for UNSCR 1803 and additional related autonomous EU measures. Resistance to quick action remains. They said that elaboration of the UNSCR 1803 concept of "vigilance" will take time due to Member State concerns regarding setting precedents, economic impact, and perceived linkages to pending legal challenges related to terrorist financing sanctions. Preliminary recommendations being considered by the EU include defining vigilance for the financial sector as "enhanced due diligence." EU Council action to finalize even previously agreed designations has been delayed, pending EU CFSP High Rep Solana's trip to Iran where he will deliver the P5 1 renewed offer. Tensions are evident both among the EU-3 and between the EU-3 and other EU Member States. The EU-3 faces a "philosophical reluctance" to go beyond UNSCRs. EU representatives raised concerns that pending U.S. legislation would only pit us against each other and help Iran. END SUMMARY.

[2](#). (S//NF) In meeting with EU officials and Member State diplomats, A/S O'Brien stressed the following points:

-- The USG is committed to the double track approach; strong sanctions are having an impact and forcing debate within the regime, which may be effective in enticing Iran to accept the diplomatic offers.

-- The EU's pending action to autonomously designate Bank Melli is important. He also underscored the importance of preventing "the next Melli" through robust interpretation of "vigilance" regarding state-owned Iranian banks operating in Europe. Treasury's main focus is on UNSCR 1803 para 10, which calls on countries to be vigilant to all Iranian banks. Financial measures must be targeted, dynamic, and flexible to account for new realities as the Iranian regime adjusts to existing sanctions. The Financial Action Task Force (FATF) statements on Iran's deficient anti-money laundering and counterterrorism finance (AML/CFT) regime further indicate multilateral consensus that Iran poses a threat to the international financial sector.

-- EU leadership has an impact beyond Europe. Other governments, particularly in the Gulf, "won't go beyond" EU actions. Thus the EU should set the gold standard for how the world's leading financial centers approach "vigilance" and other sanctions issues.

-- Iran is increasingly dependent on the euro, so EU actions have important implications. The EU should harness momentum

from the recent consensus on additional autonomous designations to seize this important opportunity for EU leadership.

-- Pressure is building within the U.S. Congress to go beyond existing sanctions frameworks. Critics in Congress are considering secondary sanctions regimes aimed at banks that facilitate intermediation for companies from sanctions-targeted countries. Treasury and State are making the case that U.S. partners are working to implement UNSCRs, so quick and expansive action by Europe could impact the political debate in the United States as well.

-- The United States stands ready to play a constructive role for aiding EU action as appropriate.

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EU-Level Implementation: Action Thus Far

13. (S//NF) EU representatives explained several of the EU-level implementation measures related to UNSCR 1803 requirements. According to Stephane Chardon, Sanctions Administrator, European Commission's DG External Relations (RELEX):

-- additional designations under the assets freeze (UNSCR 1803 OP 7) were annexed "immediately" (March 13, Commission Regulation 219/2008) by further amending the existing EU Iran sanctions package (Council Regulation (EC) No. 423/2007, as amended);

-- additional dual use items banned under 1803 were already covered by the previous EU list which "had gone the extra mile" after UNSCR 1747 was issued;

-- the EU has reached consensus in principle on the new list of additional persons and entities to be targeted autonomously; these will be added to the existing Regulation's annex once SG/HR Solana's request to hold on the draft Common Position has been lifted (COMMENT: According to the Council Secretariat, High Rep Solana requested that the EU postpone action on pending designations (including Bank Melli) until after his return from Iran to deliver the P5 1 renewed offer. Thus the earliest foreseeable opportunity for action would now be at the June 16-17 General Affairs and External Relations Council (GAERC). END COMMENT.);

-- implementation of UNSCR 1803 provisions on "vigilance" for cargo inspections, export credits, and financial institutions' activities are "still being discussed." Additional 1803 measures would change in "magnitude and scope" from the existing EU measures. Consequently, a new Common Position must be drafted (normally by the Council Secretariat on behalf of the EU Presidency) and agreed unanimously, followed by an implementing Regulation (drafted by the Commission for Council approval).

14. (S//NF) Emma Udwin, Member of Commissioner Ferrero-Waldner's Cabinet, expressed similar views, noting that the EU had acted immediately to freeze any assets within the EU of entities designated under UNSCR 1803 and that dual-use sanctions had been in place within the EU for quite some time. The remaining issues for discussion, therefore, were (i) how to incorporate new entities and (ii) how to move forward with additional EU measures that might address export credits, cargo inspections, and Iranian banks in Europe.

15. (S//NF) All interlocutors stressed the importance of distinguishing between implementation of UNSCRs and autonomous sanctions, underscoring that UNSCR implementation is easier to accomplish. All noted that a designation of Bank Melli would be considered an autonomous sanction, not/not an implementation of UNSCR 1803's vigilance requirement.

Issues Surrounding "Vigilance" Implementation

16. (S//NF) A/S O'Brien stressed the importance of implementing a strong interpretation of the "vigilance" requirement in UNSCR 1803. He acknowledged that comprehensive and decades-old U.S. economic sanctions against Iran mean that the U.S. is already in compliance with UNSCR 1803's "vigilance" obligation, but he expects that the FATF will continue discussions regarding UNSCR 1803 and the vigilance question. USEU Treasury Attache noted that FATF is one of the few international bodies in which the European

Commission holds full membership; it would be appropriate for

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the Commission to play a greater leadership role vis-a-vis the rest of the EU with this in mind.

17. (S//NF) EU interlocutors signaled a lengthy EU process for deciding how to implement 1803 vigilance measures at the EU-wide level. Renata Cvelbar-Bek, Slovenia's EU Presidency chair of the Council's main sanctions working group (External Relations or RELEX Counselors), said further measures would take time because of the Council's reluctance to set precedents. She confirmed the lack of EU political consensus on adopting an expansive or narrow ("robust or strict") interpretation of 1803 obligations. Nonetheless, the pending EU designation of Bank Melli would be a precedent-setting first step. Formal EU discussions on 1803 were suspended, but informal consultations are well underway. "If even 55 percent of the Member States favor a robust interpretation, it would be easier for the Presidency to present a proposal," she lamented. Separately, French RELEX Counselor Christophe Parisot said France expects discussions on EU implementation of UNSCR 1803 or additional autonomous measures will not begin until its EU Presidency, as significant Member State resistance remains. He noted that despite the recent consensus on additional designations, "it would be quite good if Italy moved." Commission sanctions staffer Albertus Straver noted that "Even the UK, a leading EU Member State pushing for farther reaching EU action than 1803, does not yet see clearly how to approach 'vigilance.'"

18. (S//NF) Chardon noted technical difficulties in defining vigilance and requested U.S. guidance on how UNSCR 1803 was implemented in the United States. Chardon said DG RELEX had convened an internal Commission expert Inter-Service Group on Iran; DG Internal Market and Services (DG MARKT) should take a leading role for defining "vigilance," as DG RELEX has "no clue" what the EU should do in this uncharted sanctions territory.

Other Obstacles: Context of Terrorist Financing
Legal Challenges

19. (S//NF) On financial sanctions, several interlocutors noted the EU Commission, Council Secretariat, and Member States are watching closely EU and national court proceedings and decisions related to terrorist financing sanctions. Although "there are no legal challenges yet" to the Iran sanctions, Albertus Straver (please protect), Sanctions Administrator, Commission DG RELEX predicted that someone would be "tempted if big commercial interests are at stake." He criticized that the Council has "taken its time" discussing UNSCR 1803 implementation, and credited the Commission for clarifying to EU Member States that para 10 was aimed at "ALL Iranian banks," not just Banks Melli and Saderat. The EU lacks "much precedent" for legislative measures against proliferation finance, as the current AML/CFT regime does not include provisions covering proliferation finance.

Economic Interests, the Euro, Security, and
EU Leadership

10. (S//NF) Economic interests are impeding EU unity in moving forward quickly to take additional action. Emma Udwin, Member of Commissioner Ferrero-Waldner's Cabinet, stressed the importance of "effective and efficient implementation. Here in Brussels, this means keeping the EU-3 in line with the rest of Europe." She noted that EU Member States "need to feel a full sense of ownership for what is implemented." If it appears the EU is "caving in to

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the United States or Brussels," Member States will not follow through on robust implementation, regardless of what is agreed. The Commission welcomed the enhanced offer to Iran and hopes Iran will "see the light." The EU's trade volume with Iran has fallen since the UN sanctions; "others such as China and Turkey are moving in to take up the slack." European businesses are pressuring EU decision-makers not to enact additional sanctions on Iran. Massoulie noted Dubai in particular seems to have benefited from tighter sanctions. Commission Crisis Platform Director and Deputy Political

Director Richard Wright explained some Member States' "huge sensitivities" against additional EU action, given their strong commercial ties to Iran. The UK and France have been the most prominent in pushing the sanctions process forward; others are more cautious.

11. (S//NF) O'Brien explained that the USG is engaged in active outreach to the private sector and governments in Asia and the Gulf on Iran. Treasury is seeing some encouraging signs of hesitance by key players in the Gulf and in Asia to capitalize on the business opportunities presented by European and U.S. measures against Iran. The UAE has quietly reached out to its financial sector, and the international market has tightened letters of credit. He noted that other governments look to the EU as the minimum standard for implementing restrictive measures, thus, additional vigorous EU action is essential. Furthermore, Iran cannot adequately substitute European technology and expertise, which are essential to key Iranian infrastructure projects, such as natural gas extraction. Iran has moved out of dollar and into euro-based transactions; the regime's dependency on this currency should not be underestimated. O'Brien said the United States would welcome the EU's joining our outreach to regional actors to stress the importance of taking action. EU interlocutors seemed relieved to learn about U.S. outreach efforts to China and others, and took the point that the EU was setting a model for other country's decisions. Massoulie said outreach to China, Asia, and other eastern actors could help respond to the legitimate concerns being raised by the EU business community.

Sanctions Skepticism, Evidence of Impact?

12. (S//NF) Cvelbar-Bek explained that political discussions on how far to go with Iran sanctions are tied up in general concerns about how far the EU should go with autonomous sanctions, most recently regarding Burma. If the EU acts without the rest of the UN, will there really be an effect? Won't the targeted country just switch its business to another state? How will it affect the local and civilian population?

13. (S//NF) On the impact of sanctions on Iran, O'Brien explained that foreign direct investment has decreased. Iran is struggling to finance infrastructure projects and is increasingly isolated from the international financial system. Iran's cost of doing business is rising because of increased political and commercial risk. Debate is taking place in Iran, with key politicians and departing ministers speaking out about the impact of the regime's economic troubles and mismanagement. Though most of Iran's economic troubles are most appropriately attributed to the government's own mismanagement, sanctions targeting specific institutions are also having a dissuasive impact on behavior.

A Divided EU and Cracks Apparent in the EU-3

14. (S//NF) Udwin warned that the international coalition must hold together. She noted that the EU-3 is not operating

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with an actual EU mandate, and are often not in line with the rest of the Member States. The Commission's role is to make proposals for implementation serving an EU consensus only: "There are limits to how far we can push." Commission staff work to make sure a proposal is ready at the first moment it can be accepted unanimously. Massoulie noted that "most" Member States accept the de facto EU-3 "when they act as partners." If the EU-3 negotiates with the U.S., Russia, and China, the other Member States always support this multilateral effort as backing the UN Security Council. But when the EU-3 tries to push for autonomous EU measures, "there is NEVER an appetite." The EU-3 may make robust arguments, but the pervasive belief remains that UNSC action is necessary. Massoulie further warned that the previously strong unity among the UK, France, and Germany has been weakening since the beginning of 2008. Unity remains strong only "between the UK and France. Now Germany's position is slightly more nuanced, adding a new element of complexity." O'Brien commended the EU for having made progress to work past the issues raised by Italy, Spain, and others, and stressed that for financial measures to be effective, some sacrifices must be made.

Prospects for French EU Presidency:

¶15. (S//NF) Meeting bilaterally with French representatives, O'Brien asked whether France had any suggestions for how the United States could be helpful in pushing for a vigorous EU interpretation of UNSCR 1803. O'Brien noted that the USG had shared thoughts with the UK and France regarding implementation of paragraph 10 of UNSCR 1803, and expressed hope that the three countries could agree on a plan that could be presented to other countries and multilateral organizations such as the FATF.

¶16. (S//NF) Speaking "frankly and honestly," French RELEX Counselor Christophe Parisot cautioned that EU Member States bristle when the U.S. appears to be inserting itself into EU policy making. The U.S. could be helpful in "giving input about how you do it and exchanging views on how you see sanctions," including at the financial level, the U.S. dynamics for controlling cash flows (as opposed to the static EU freezing approach), and concrete measures taken to apply UNSCR 1803. Parisot warned that if the EU-3 are not united at this stage or are unable to propose concrete texts for discussion, there is "no way" the other Member States will favor a robust interpretation. He conceded that the lack of unity was not very helpful, and that Germany has been wavering. Getting the Melli designation right ASAP is clearly key. Deputy PSC Ambassador Didier Chabert stressed the importance of engaging Germany, Italy, and Spain. Frederik Rogge, French counselor for the Middle East and Gulf, added that EU Member States certainly will ask about the "incentive and dialogue side" when discussing options for further measures.

Comment

¶17. (S//NF) The EU process for implementing UNSCRs generally and making autonomous designations specifically seems to be losing momentum. The Commission seemed to register the message that the U.S. and the EU should work toward a common view on how to best interpret "vigilance" when implementing UNSCR 1803. It is less clear whether all interlocutors accepted the need to act urgently to overcome Member State political and economic resistance, and whether the Commission has either the ability or the authority to affect the debate.

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¶18. (S//NF) Defining best practices on "vigilance" in FATF could be a useful avenue to trigger forward progress in Europe. The USG should continue the proactive but low-key, "behind the scenes" approach of engaging key allies (France, UK) in sharing ideas for the EU's potential interpretation of vigilance. USEU has shared liberally the 60-Day report with various EU geographic and sanctions contacts (Commission, Council Secretariat, Presidency, Member State) in hopes of influencing EU institutional thinking on defining "vigilance." If necessary, USEU will request additional engagement from USG experts to clarify any questions arising from the EU side about how to approach and implement financial sanctions regimes.

¶19. (S//NF) The USG should ask the French how they plan to use their Presidency to influence EU dynamics regarding financial sanctions starting July 1. EU Presidencies are traditionally somewhat constrained in promoting strong national views at EU level, but this issue might be an exception to that rule. On the margins of the May 21-22 U.S.-EU sanctions workshop, the French sanctions representative told USEU that a final EU deal on the next round of measures will require mainly a consensus among five key members: UK, France, Germany, Italy, and Austria. The rest would fall in line once these had agreed, he predicted. The USG should continue targeted outreach efforts with these countries in mind. END COMMENT.

¶20. (U) A/S O'Brien has cleared this message.

¶21. (U) MINIMIZE CONSIDERED.

MURRAY
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